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## **SOCIO-ECONOMIC FACTORS INFLUENCE ON FOREIGN DIRECT INVESTMENT (FDI): A COMPARATIVE STUDY OF INDIA AND VIETNAM**

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### ***ABSTRACT***

Foreign capital plays an aiding role in the economic development of a nation. Foreign direct investment (FDI) is viewed as a driving factor for economic growth. This paper investigates the role of socio-economic factors in India and Vietnam, and explains the influx of Foreign Direct Investment (FDI). In this analysis uses data from cross section time series for 15 socio-economic factors and the study period is from 1997 to 2018. Our empirical results are that the relationship of importance between variables and FDI flows in. In the last few years, because of data limitations, the literature review had concentrated on total FDI inflows in

Asian countries. Unemployment and inflation have had a significant positive effect on both India and Vietnam's FDI inflows.

**Keywords:** *FDI Inflows. Socio-economic variables, Time series, India, Vietnam, Co-integration*

**JEL Classification:**F21

### **Introduction**

Evidently, Foreign Direct Investment (FDI) has been attributing economic progress from the experience of the global economy. Foreign Direct Investment not only impacts the host country's wealth, but also aims to enter new markets, develop state-of-the-art technologies and skills, and produce revenue. FDI contributes to finding viable solutions for a number of concerns. FDI provides useful resources for stimulating economic growth and development, and introduces awareness to technology.

In addition to the initial macroeconomic stimulus from real investment, FDI affects development by increasing the competitiveness of the total factor and, more generally, the quality of resource usage in the beneficiary economy. This operates across three channels: the relations between FDI and foreign trade flows, the spillovers and other externalities to the host country business sector and the direct effect on the host economy's structural factors. Most empirical studies conclude that in host countries, FDI contributes to both productivity and sales growth factors, beyond what would usually cause domestic investment.

FDI tends to have a much lower impact on development in the least developed economies, due to the lack of 'threshold externalities.' Developing countries apparently need to have achieved a certain level of growth in education, technology, infrastructure and health before they can benefit from a foreign presence in their markets. Imperfect and underdeveloped financial markets can also impede a country from taking full advantage of FDI. Poor financial intermediation is affecting domestic companies even harder than multinationals (MNEs).

The willingness of host countries to use FDI as a means of growing exports in the short and medium term depends on the context. The clearest

examples of export enhancing FDI are found where inward investment helps financially stressed host countries make use of either their resource endowment (e.g. foreign investment in mineral extraction) or their geographic position (e.g. investment in some transition economies). Targeted initiatives to leverage the benefits of FDI to incorporate host economies more tightly into international trade flows have attracted growing attention, notably through the establishment of export-processing zones (EPZs).

During the last two decades, Vietnam has succeeded in attracting a massive inflow of inward foreign direct investment (FDI), which together with trade liberalization has made a significant contribution to Vietnam's economic growth (Le Dang Doanh 2002. Dollar 1996; Dollar and Kraay 2004).

According to official statistics the contribution of the FDI sector in Vietnam economy is significant and getting more and more important. In 2000, the contribution of the FDI sector to GDP was about 13.2 percent, and increased to 17.9 percent in 2015.

The International Monetary Fund (IMF) reports that, FDI is classified as an investment which operates in an economy other than the investor's. The aim of the investor is to have an influential voice in enterprise management (IMF, 1977). FDI is the mechanism through which citizens of one country (the source) gain ownership of assets for the purpose of manufacturing power. Distribution and other productive activities of a business in another (host) country.

### **Literature Review**

Since the 1960s various definitions have been developed to describe FDI. Such definitions proclaim a variety of determinants that could describe the foreign direct investment flows in terms of micro and macro linking economic factors. The micro dimension involves factors which are integral to the firm itself. As for the benefits of possession. Cost reduction and Scale Economies. Whereas the macro aspect concerns specific market conditions, such as entry barriers. Resource Accessibility. Stability diplomacy. Country risk, and size of the market. Among others.

Researchers have concentrated on the macro and micro impacts of various aspects of FDI inflows towards economic growth.

The institutional investor country risk rating was evaluated by Janicki and Wunnava (2004) and they provided evidence that established risk reduces FDI receipts. Kinoshita and Campos (2003) tested evidence that significant FDI drivers are the rule of law and the consistency of the bureaucracies. On the other side, they found the FDI restrictions to be an effective barrier to FDI inflows.

Arabi and Agarwal (2005) (2001). In India, FDI remained finding the domestic market. It is widely believed that the FDI form and its structural composition are at least as important for the effects of economic growth as is the overall amount of inward FDI.

According to Agrawal and Shahani (2005), it is the standard of FDI that matters to a country like India rather than its quantity. Often, FDI should be of higher quality if it is targeted towards export. Transfers to the host country of international technologies; And it causes economic spillovers that favor local businesses and workers (Ender wick 2005).

FDI is supposed to accelerate, or contribute, to all countries ' economic growth. For several past years, the connection between FDI and economic growth has been a subject of great debate. Monhanty et al (2007) explored the interrelations between the FDI variables. And the four countries imports and exports. Chinese. Asia. India. Malaysia-Malaysia. And Singapore, using Panel Data Analysis techniques. Their report indicated that the FDI is promoting economic growth. Provided an estimate contributing about \$3.27 to the GDP of each of the four countries on the dollar of FDI. Narayana *et al.* (2008). analysed theoretically India's economic growth and the role of FDI. They showed the comparative analysis of the Indian and Chinese economy.

Elboiashi and others. (2009). The causal relationship between FDI has been investigated. In Egyptian Domestic Investment (DI) and Economic Growth (GDP). The Economies of Morocco and Tunisia. They applied the techniques of time series co-integration. Model Vector Error Correction (VEC) over the 1970–2006 sample period. They consider in Egypt and

Morocco an unidirectional causality between the FDI and GDP. And bi-directional causality in Tunisia, between FDI and GDP.

Merican (2009) tested the impact of FDI and Gross Domestic Investment on growth in case of four Asian countries. suggested that the FDI is better than Domestic Investment for growth only in two countries.

Yusop and Karimi (2009). Basing on a simple regression of OLS. Studied the Growth-FDI case in Malaysia. Depending on the writers. There are a number of possible reasons to ensure that FDI facilitates economic growth or hinders it.

Wang et al. (1999). Examined the FDI and GDP logistics in two dimensions of China's time series and growth rate. Empirically, they found that logistical FDI improved the quality of foreign investment and supported the change in China's economic growth pattern to ensure China's economy's progress.

Mohamed Azam. The determinants of Foreign Direct Investment in India were analysed by Ling Lukman (2010). Indonesia, and that of Pakistan. The authors of this research paper plan to examine the factors that deter and promote the inflows of FDI into Pakistan. India and Indonesia ranged between 1970 and 2005 during the study period. We also analyzed the patterns and significance of FDI inflows into the countries selected. Log linear regression model was used, and the least square approach was used to estimate the various effects of economic determinants on FDI inflows.

Agrawal et al. (1999). Researched the effect of the FDI on China and India's economic growth. They researched possible reasons behind China's great FDI series, and the lessons India should learn from China to make better use of FDI.

Bose (2012) researched the identification of positive and negative sides for foreign investors as they go to India and China for direct investment. A descriptive and exploratory analysis study was conducted to examine the proposed FDI case proposal in the two countries concerned.

Devajit (2012) has empirically tested how FDI, by increasing domestic investment, is seen as an important economic driver of Indian economic growth. Rising the development of human capital, and

promoting transfer of technology.

Trinh and Nguyen (2015) reports that long-term economic growth in Vietnam is correlated with a one percent increase in FDI. By using panel data covering 61 Vietnam province during the period 1996-2005.

Seng (2016) used panel data for 21 Asian countries and found that a 1 percent increase in FDI and exports resulted in Vietnam's long-term economic growth of 0.334 per cent and 1.438 per cent respectively. Likewise. Using annual data series for the 1990-2013 period.

### **Objectives of Study and Contribution of the Study**

To investigate the effects of socio-economic variables on Indian and Vietnam Economy FDI inflows. This study attempt should yield results related to the cause and effect of the state of the economy. This will, in other words, contribute to an understanding of the relationship between socio-economic indicators and FDI inflows.

### **Methodology**

#### ***Data***

Indian Data has been obtained from the Reserve Bank India (RBI) and Department of Industrial Policy and Promotion (DIPP), and World Bank data official website. Vietnam country data were obtained from the World Bank official website. UNCTAD and General Statistics Office of Vietnam. The secondary data alone used for this study. The Macro variables are considered for this study namely Population, Literacy rate, Improved Sanitation, Improved Water Source, Population living Slums, CO2 emissions, Unemployment, Prevalence of Undernourishment, Household Final Consumption, Import of Goods, GNI Growth, Gross Domestic Savings, Inflation, GDP Per Capita, and Gross Domestic Savings.

The study period was from 1997 to 2018. The major objective of this paper is to analyze the impact of FDI inflows. Initially, as a benchmark. We calculated the impact of overall FDI inflows on economic growth based on the following equation. Presentation the results for the estimation that uses only FDI inflows and socio-economic factors, following:

$$\ln FDI = \alpha + \beta_1 POP + \beta_2 LIT + \beta_3 SAN + \beta_4 WAT + \beta_5 SLU + \beta_6 CO2 + \beta_7 UNE + \beta_8 UN + \beta_9 HFC + \beta_{10} IMP + \beta_{11} GNI + \beta_{12} \ln GDS + \beta_{13} \ln INF + \beta_{14} \ln GDP + \beta_{15} \ln GSS + \varepsilon$$

**The Error Correction Representation**

The long-run coefficients calculation and the final step is Error correction term

$$H_0 = \delta_1 = \delta_2 = 0 \text{ (no cointegration)}$$

$$H_1 = \delta_1 = \delta_2 \neq 0 \text{ (cointegration)}$$

The rejection and acceptance of the null and alternative hypothesis depend on the value of F statistics and the critical values calculated by Pesaran et al., (2001). The null hypothesis will be accepted in case of F test value falls below than the lower bound, and we accept the alternative hypothesis if the F test value is greater than the upper bound. After confirming of the co-integration we can proceed to the long run coefficient estimation and in the third stage the error correction term of the ARDL model. The general model of the ARDL approach and error correction is given below.

$$\ln FDI = \sum \alpha \ln FDI_{t-1} + \sum \beta_1 POP_{t-1} + \sum \beta_2 LIT_{t-1} + \sum \beta_3 SAN_{t-1} + \sum \beta_4 WAT_{t-1} + \sum \beta_5 SLU_{t-1} + \sum \beta_6 CO2_{t-1} + \sum \beta_7 UNE_{t-1} + \sum \beta_8 UN_{t-1} + \sum \beta_9 HFC_{t-1} + \sum \beta_{10} IMP_{t-1} + \sum \beta_{11} GNI_{t-1} + \sum \beta_{12} \ln GDS_{t-1} + \sum \beta_{13} \ln INF_{t-1} + \sum \beta_{14} \ln GDP_{t-1} + \sum \beta_{15} \ln GSS_{t-1} + \mu_t$$

$$\ln FDI = \sum \alpha \ln \Delta FDI_{t-1} + \sum \beta_1 \Delta POP_{t-1} + \sum \beta_2 \Delta LIT_{t-1} + \sum \beta_3 \Delta SAN_{t-1} + \sum \beta_4 \Delta WAT_{t-1} + \sum \beta_5 \Delta SLU_{t-1} + \sum \beta_6 \Delta CO2_{t-1} + \sum \beta_7 \Delta UNE_{t-1} + \sum \beta_8 \Delta UN_{t-1} + \sum \beta_9 \Delta HFC_{t-1} + \sum \beta_{10} \Delta IMP_{t-1} + \sum \beta_{11} \Delta GNI_{t-1} + \sum \beta_{12} \Delta \ln GDS_{t-1} + \sum \beta_{13} \Delta \ln INF_{t-1} + \sum \beta_{14} \Delta \ln GDP_{t-1} + \sum \beta_{15} \Delta \ln GSS_{t-1} + \mu_t$$

**Results and Discussion**

**Variance Inflation Factor (VIF) Results (Refer Table No – 1 and 2)**

Exhibits from Table No.1 and 2. For the initial model building the nine variables were considered and six variables were rejected due to high VIF. Socioeconomic factors out of the fifteen variable five considered with

the notation of the initial level consideration for the proposed model, namely Improved Sanitation (San), Living Slum Population (Slu), Under-Nourishment Prevalence (Nou), Gross Domestic Savings (GDav), and Gross Savings (GDav) (GSav). According to the VIF outcome basis, four variables considered for the model are Co2 emissions (Co2) unemployment rate (Une), GNI growth (GNI), and inflation (Inf). Five variables are considered with high notation, namely Literacy Rate (Lit), Co2 Emissions (Co2), Unemployment Rate (Une), GNI Growth (GNI), and Inflation (Inf), as the proposed model for Vietnam

#### **ADF Test Results (Refer Table No – 3 and 4)**

Table- 3 & 4 reports the results of ADF test. It is clear from the results that the variables Unemployment (Une) and Inflation (Inf) are stationary at level in the India, the Vietnam country the variables Population in Living Slums (Slu), Inflation (Inf), and Gross Domestic Savings (GSav) are stationary at level while the remaining variables are non-stationary. Mix order of stationerity is reported, therefore, Autoregressive Distributed Lag Model is adopted for estimation. The first step in ARDL methodology is the investigation of long run relationship existence.

#### **Regression Co-efficient (Refer Table No – 5. 6 and 7)**

Our key finding is that FDI's optimistic value flows with socio-economic variables. FDI plays a positive role for the FDI in stimulating both countries ' economic growth. The R-square value of the contributing socioeconomic variables as a whole is 0.791 as per model-1. Resident societies Slums, CO2 pollution, Domestic Savings, and Gross Savings have a VIF greater than 10. Four variables need to be removed from the model to put in the best linear model. Model 2 puts out variables with the best fit. The ratio to R-square is 0.645. DW numbers are inferior to 2 which imply a model free of the question of collinearity. The effect of unemployment and inflation on India's FDI inflows has been important. A negative relationship with FDI Inflows has been identified with prevalence under nourishment and domestic savings. For the country Vietnam the regression results has shown R square value is 0.66. The macro variables Population living Slums, and Gross Savings were shown the negative



significant at 5 per cent and 1 per cent level respectively. The model 1 of Vietnam does not have any collinearity problem. Since the VIF lies less than 10 and DW statistic is shown value less than 2. Regression Result of India, the Model-2 which used for further prediction and Model-1 Regression result of Vietnam is used to estimate the long-run equilibrium estimate. (Error Correction Estimates)

#### **Error Correction Model Estimate Results (Refer Table No – 8 and 9)**

It demonstrates the results of short-term forecasts and the speed of equilibrium change. It is clear from the table that expects all variables to be significant D(GDPG). The proposed model for India (model 2) and Vietnam (model 2) was tested using the Model for Error Correction (ECM). The ECM test results for India, the error correction coefficient (ECt) is -0.857, and the likelihood value is 0.000, which is important. The term error correction coefficient implies that, after a short-run deviation, foreign direct investment returns to its long-term equilibrium at a rate of 85 per cent in one year. The test results of Vietnam on ECM, the Error Correction (ECt) coefficient is -0.787 and the probability value is 0.000, which is an important coefficient suggesting that the foreign direct investment returns to its long-run equilibrium with a pace of 78% in one year after a short-run deviation. D(GNI) is not significant, except that all the variables contribute significantly to the long-term equilibrium formed.

#### **Conclusion**

For many developing countries attracting foreign direct investment (FDI) has become an important component of economic and industrial growth strategies. India and Vietnam aren't excellent countries. This paper notes that two countries' socio-economic growth is influenced by FDI in flows in India and Vietnam. Most of the theoretical work on the FDI-related benefits appears to be tied to the growing economy. Because of data limitations, the literature review had concentrated on total FDI inflows in Asia countries. Unemployment and inflation have had a significant impact on both India and Vietnam's FDI inflows. This research attempts suggests that not all forms of foreign investment seem to be beneficial to Indian and Vietnam economy. The entire framed model is lies within the error limits.

We can conclude that framed is suitable for future forecasting. Further researches can be done with possible improvements with this model.

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**Table -1: Multi Collinearity Statistics on India Socio Economic Factors**

<b>Variables</b>	<b>Tolerance</b>	<b>VIF</b>	<b>Decision</b>
Population (Pop)	0.000	68247	<b># Not Considered for Model</b>
Literacy Rate (Lit)	0.016	63	<b>*Initial Level Consideration</b>
Improved Sanitation (San)	0.000	27661	<b># Not Considered for Model</b>
Improved water Source (Wat)	0.000	104494	<b># Not Considered for Model</b>
Population in Living Slums (Slu)	0.012	83	<b>*Initial Level Consideration</b>
Co2 Emissions (Co2)	0.010	99	<b>***Highly Considered</b>
Unemployment Rate (Une)	0.061	16	<b>**Considered</b>
Prevalence of Undernourishment (Nou)	0.044	23	<b>*Initial Level Consideration</b>
Household Final Consumption (Con)	0.000	4911	<b>#Not Considered for Model</b>
Imports of Goods (Imp)	0.001	727	<b>#Not Considered for Model</b>
GNI Growth (GNI)	0.132	8	<b>***Highly Considered</b>
Gross Domestic Savings (GDav)	0.004	223	<b>*Initial Level Consideration</b>
Inflation (Inf)	0.050	20	<b>***Highly Considered</b>
GDP Per Capita (GDP)	0.000	7321	<b>#Not Considered for Model</b>
Gross Savings (GSav)	0.024	43	<b>*Initial Level Consideration</b>

Note: In Bracket ( ) Abbreviation of variables defined

**Table 2: Multi Collinearity Statistics on Vietnam Socio Economic Factors**

<b>Variables</b>	<b>Tolerance</b>	<b>VIF</b>	<b>Decision</b>
Population (Pop)	0.000	35614	<b># Not Considered for Model</b>
Literacy Rate (Lit)	0.052	19	<b>**Considered</b>
Improved Sanitation (San)	0.000	250148	<b># Not Considered for Model</b>

Improved water Source (Wat)	0.000	201709	# Not Considered for Model
Population in Living Slums (Slu)	0.024	42	*Initial Level Consideration
Co2 Emissions (Co2)	0.119	8	***Highly Considered
Unemployment Rate (Une)	0.066	15	**Considered
Prevalence of Undernourishment (Nou)	0.001	1158	# Not Considered for Model
Household Final Consumption (Con)	0.000	3845	#Not Considered for Model
Imports of Goods (Imp)	0.003	301	#Not Considered for Model
GNI Growth (GNI)	0.115	9	***Highly Considered
Gross Domestic Savings (GDav)	0.000	2061	#Not Considered for Model
Inflation (Inf)	0.118	9	***Highly Considered
GDP Per Capita (GDP)	0.000	9131	#Not Considered for Model
Gross Savings (GSav)	0.015	69	*Initial Level Consideration

Note: In Bracket ( ) Abbreviation of variables defined

**Table 3: ADF Test Results on Considered Variables of India as per Model -1**

At Level			At First Difference		
Variables	T-Static	P-Values	Variables	T-Static	P-Values
Ln FDI	-0.772	0.813	Ln FDI	-4.141	0.005*
Slu	2.180	0.217	Slu	-3.740	0.008*
Co2	-1.742	0.397	Co2	-3.621	0.016**
Une	-1.325	0.050**	-	-	-
Nou	-1.866	0.324	Nou	-4.912	0.000*
GNI	-1.137	0.668	GNI	-4.824	0.000*
DSav	-2.568	0.109	DSav	-5.817	0.000*

Inf	-2.984	0.049**	-	-	-
GSav	-1.474	0.526	GSav	-4.12	0.002*

**Note:** \* and \*\* represents the level of significance at 1 and 5 percent respectively. The series regression equation includes only for intercept

**Table 4: ADF Test Results on Considered Variables of Vietnam as per Model -1**

At Level			At First Difference		
Variables	T-Static	P-Values	Variables	T-Static	P-Values
Ln FDI	-0.557	0.854	Ln FDI	-3.442	0.005*
Lit	-1.879	0.557	Lit	4.001	0.007
Slu	-2.221	0.051**	-	-	-
Co2	-1.742	0.397	Co2	-3.621	0.016*
Une	-1.452	0.452	Une	-3.007	0.002*
GNI	-1.137	0.668	GNI	-4.824	0.000*
Inf	-3.184	0.050**	-	-	-
GSav	-2.101	0.042**	-	-	-

**-Note:** \* and \*\* represents the level of significance at 1 and 5 percent respectively. The series regression equation includes only for intercept

**Table 5: - Model – 1**

**Socio-Economic Factors Impacts in Foreign Direct Investment (FDI) Inflows of India**

Source	Value	t	Pr>  t	VIF	R-Squared	Adjusted R-Squared	DW Statistic
Intercept	15.666	0.586	0.571		0.791	0.603	4.980
Lit	0.166	0.046	0.965	6.631			
Slu	-2.109	-1.151	0.276	18.592*			
Co2	-1.931	-0.384	0.709	13.157*			
Une	0.438	0.558	0.589	4.832			
Nou	-1.162	-0.631	0.542	6.755			

GNI	-0.015	-0.044	0.966	1.975			
DSav	-0.468	-0.937	0.371	19.371*			
Inf	0.278	0.558	0.589	7.341			
GSav	3.037	1.273	0.232	15.798*			

\* VIF (Variance Inflation Factors) – minimum possible value – 1.0, and value >10.00 may indicates a collinearity problem.

**Table 6: Model – 2**

**Socio-Economic Factors Impacts in Foreign Direct Investment (FDI) Inflows of India**

Source	Value	t	Pr>  t	VIF	R-Squared	Adjusted R-Squared	DW Statistic
Intercept	-13.217	-0.997	0.336		0.645	0.518	1.328
Lit	0.309	1.201	0.250	2.600			
Une	0.598	3.231	<b>0.006</b>	1.350			
Nou	-0.204	-0.813	0.430	2.489			
GNI	0.217	1.225	0.241	1.243			
Inf	0.503	2.625	<b>0.020</b>	1.449			

Note: bold in number indicates the significant condition (Pr>|t)

**Table 7: Model - 1**

**Socio-Economic Factors Impacts in Foreign Direct Investment (FDI) Inflows of Vietnam**

Source	Value	t	Pr>  t	VIF	R-Squared	Adjusted R-Squared	DW Statistic
Intercept	18.810	0.485	0.637		0.666	0.471	1.880
Lit	0.213	0.011	0.991	6.329			
Slu	-1.622	-2.175	<b>0.050</b>	5.808			
Co2	-0.607	-0.382	0.709	1.658			
Une	1.405	1.989	0.070	2.732			
GNI	-0.483	-1.418	0.182	1.406			
Inf	0.477	2.115	<b>0.056</b>	1.258			
GSav	-2.923	-4.231	<b>0.001</b>	2.663			

Note: bold in number indicates the significant condition (Pr>|t)



**Table 8: (Based on Model 2)**  
**Error Correction Representation Socio-Economic Factors and Foreign Direct Investment (FDI) Inflows of India**

Variable	Coefficient	Std. Error	T-Statistic	Prob.
D(Ln FDI (-1))	1.816	0.873	2.08018**	0.04
D(Lit(-1))	2.181	0.616	3.54058*	0.01
D(Une)	-1.74	0.494	3.52227*	0.01
D(Nou(-1))	1.862	0.541	3.44177*	0.01
D(GNI(-1))	1.869	0.488	3.82992*	0.01
D(Inf)	-1.353	0.592	-2.28547**	0.04
Ect(-1)	-0.857	0.062	-13.82225*	0.00

Note; \*, \*\*, \*\*\* the level of significance at 1%, 5% & 10% respectively.

**Table 9: (Based on Model - 1)**  
**Error Correction Representation Socio-Economic Factors and Foreign Direct Investment (FDI) Inflows of Vietnam**

Variable	Coefficient	Std. Error	T-Statistic	Prob.
D(Ln FDI (-1))	0.230283	0.0105077	15.27334*	0.00
D(Lit(-1))	0.794382	0.28134	2.420907**	0.01
D(Slu)	-0.034212	0.00521	-6.734741*	0.01
D(CO2) (-1))	-0.621112	0.10511	-5.90331*	0.01
D(Une) (-1))	-0305111	0.05300	-5.70711*	0.01
D(GNI(-1))	0.01211	0.01500	0.79701	0.47

D(Inf)	-0.00951	0.01611	-5.73911**	0.04
D(G Sav)	0.50411	0.27921	1.80112***	0.10
Ect(-1)	-0.787	0.0482	-16.32781*	0.00

Note; \*, \*\*, \*\*\* the level of significance at 1%, 5% & 10% respectively.